

# Physician Business Strategies For an Era of Managed Care

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Managed care, for better or worse, is here to stay. As proof, consider the fact that managed care enrollment continues to rise in all product lines, from commercial products to senior care products and now even Medi-Cal.

Exacerbating the challenge for practicing physicians is the fact that our medical schools continue to crank out students eager to plunge into a crowded pool of professionals. In Southern California, for example, we already have three times the number of specialists needed to serve the population, and twice the necessary number of hospitals.

As in any supply and demand equation, this oversupply means a financial hit for the seller (physicians) and a cost reducer/cash generator for the buyer (IPA's, HMO's, and other managed care organizations).

What can you do? Is there a way you can maintain your practice and your income in the face of what looks like a smart bomb dropped in the pipeline of traditional medicine? Yes-and in this special report, I'll share several specific strategies for making your practice thrive and even improving your financial position in an era of managed care.

Our organization, Medical Pathways, serves many doctors and groups who are successfully adjusting to today's managed care environment. Here and there, I'll include a few "TIPS" for very specific strategies which are based on our direct experience.

What trends is managed care producing? And how do these affect your practice? Let's take a look at some key factors driving medical economics today.

## **1. Innovation.**

Today's physicians are pressed to find quicker, faster, cheaper ways to get the same result. Where a doctor, a nurse and an assistant might have once taken half an hour to wrap a cast, today a plastic cast can be put on in less time by an assistant who's paid less than half a nurse's salary. The result, if anything, is better. Similarly, today dermatologists use laser surgery to remove warts in a fraction of the time with less scarring.

## **2. Growth in Medical Practice Groups.**

Growth in Medical Practice Groups. A group practice brings many economies of scale to its members. Doctors typically share information systems, administrative staff and other services. The overhead for each doctor is less. But the most important factor in the growth of groups is that HMO's and IPA's prefer to do business with groups...because of reduced paperwork, improved oversight, additional access and broader services.

## **3. Reduction in Compensation.**

Until recently, doctors could count on plenty of referrals at fees that they established for themselves. Today, the referrals come through managed care and fees are set. The most dramatic price constraint is a capitation contract, in which specialists charge a fixed amount per patient to cover all patients in the group who need care in that specialty.

TIP: Before assuming that capitation automatically means less revenue, do the math. Remember to factor in the number of patients you see each month. If you end up with less revenue but see fewer patients, that probably means you have extra time available to see new patients on a fee basis. (How do you get those new fee-based patients? See below.)

#### **4. Increase in Outpatient Care.**

Physicians and hospitals are directed by managed care organizations to get patients out the door quicker, or in many cases to have a process which avoids admitting non-acute cases in the first place. Less invasive surgical procedures help to make this possible. Outpatients do not need a bed and use far fewer support services than patients who are hospitalized. But many doctors find they are expected to lower their fees as part of the package, even when the procedure performed is exactly the same whether the patient is hospitalized or not.

#### **5. Higher Levels of Patient Service Accountability.**

Because HMO's and IPA's are businesses, they like to measure results. Surveys which indicate happy patients are one such measurement. Many groups now survey their patients on issues like: how long does it take to get an appointment? To see a doctor? For surgeons, what is the rate of re-dos and infections? I know of one instance where a group won a large contract even though it was the highest priced bidder, on the basis of its patient satisfaction and proof of conscientious utilization. This is an extreme example, but it certainly shows the importance of measuring results and being able to document patient satisfaction.

TIP: If you do business with IPA's, consider initiating your own patient satisfaction survey. Ask patients how they feel about their experience with your practice, and then correlate with any available clinical statistics. This helps to differentiate you from other clinical practices, and could lead to more contracts. What are the commonalities in all these trends? Medicine has become a business. And the primary focus of those who are paying for it (usually employers who are members of a health plan) is cost. This means the most successful physicians will be those who treat their practice as a business, and aggressively defend their bottom line. They will seek out contracts, they will manage efficiently to reduce operating costs, and they will guard their "accounts" (patients) like any other enterprise. Let's look at some strategies.

### **Five Scenarios to Make Your Practice Thrive in an Era of Managed Care**

#### **1. Build a Reputation for Fee-Based Services.**

One good thing that managed care has introduced is a new awareness of how much services cost, which leads logically to asking how much those services are worth. Until recently patients didn't care about costs because they never saw the bills. Today, patients are acutely aware of what their plan does and does not cover. And some of these patients willingly pay out of their own pocket for the best possible care because they recognize it's their own health at stake. For example, I know a dermatologist whose fees are capitated per patient per month, but whose patients often request services which are not covered by their insurance. Instead of turning them away as many physicians might, this doctor performs the additional service on a fee basis and adds substantially to his income.

#### **2. Seek Referrals from Your Patients.**

Patients in an HMO or PPO receive a list of "approved" doctors with little guidance other than the specialty description. How do they make a choice? Very often, by relying on referrals from other people in the plan, typically their co-workers. By keeping your patients happy and letting them

know you welcome referrals, you'll maximize your opportunities through this avenue-first by allowing you to fill out your contracts, then through potential fee-based services from these new patients.

TIP: Referrals from patients in a managed care plan can ultimately be more lucrative than referrals from other physicians because of the sheer numbers involved.

### **3. Go After Managed Care Contracts.**

In many communities, managed care organizations cover 50% or more of the population. That means a doctor who decides not to work with managed care is immediately cutting his or her potential patient base by half. Very few enterprises can afford that kind of financial hit. That's why I suggest you need to pursue managed care contracts.

How do you get the contracts? Call the major IPA's, HMO's, health plans and other managed care organizations in your area and ask how you can get on their list of approved physicians. They may say they already have enough doctors in your specialty, so be prepared to do some selling. Is there a regular interval at which they put contracts out for bid? Can you get recommendations from influential decision makers, such as people on the board or doctors in the plan who will make referrals to you?

TIP: If it sounds like I'm suggesting drastic measures, it's because the managed care environment requires them. The doctor who has no managed care contracts today is at a disadvantage. One strategy you might consider would be to go to a group which already has contracts and offer a merger in which you bring them your business and they allow you to participate in their contracts.

### **4. Join or Merge with a Successful Group Practice.**

The game plan is this: hire (or contract with a management company to secure) a strong and motivated administrator. Consolidate multiple practices into a single, integrated group. Follow a single, unified business plan. This strategy takes on the challenge of managed care and comes out a winner with a single- managed, multi-site, area-wide organization that can deliver quality within the budgets available. For it to succeed, however, emphasis must be placed on efficiency of operations. If you're not careful, size and complexity can increase overhead and thus reduce profits or compensation. Make sure your long term business plan charts a course for economies of scale in purchasing, increasing quality through specialty and sub-specialty services and expertise, and higher levels of management expertise and systems to better manage for revenue growth and operations productivity.

TIP: Increased costs may be inevitable during the startup phase (first two years) of a merged or new practice, but after that the new economies of scale should quickly repay your investment.

### **5. Join Forces with a Capital Partner.**

Corporations often become merger candidates when they are long on expertise and short on operating or expansion capital. Physicians can benefit from the same strategy. Capital practice partners bring access to financial resources and management depth which are simply unavailable to smaller groups. They also bring stock option plans, appreciating stock prices, negotiations clout, attractive clinic sites, state-of-the-art information systems, business discipline and vision.

Practice management capital partners have only emerged in the past several years. They have grown quickly; Wall Street is supportive; and they will provide an attractive practice growth strategy to more and more physicians in the future.

## 6. What About Selling Your Practice?

If you're somewhat close to retirement age and accustomed to doing business in the pre-managed care era, you may be thinking you will do things as you have all along and then sell your practice and retire. How much will your practice be worth at that time?

The good news is that the economics of valuing a practice haven't changed...the price is still based on what it is worth in potential revenue to a buyer. But once again, there are new considerations in the new world of managed care. If you have a sizable managed care contract, and it can be transferred, that will add to the value. But if most physicians in your area have managed care contracts and you don't, the value of your practice may be lowered even if you have a solid patient base today.

Today's economic buyer will also look at your potential profit margin, as well as the trend of your revenues. It's important to keep this in mind. The standard operating procedure has been to "bonus" the profit out of the practice to yourself and your partners. Under a sale, however, you will need to bring a demonstrable profit to the buyer.

TIP: Medical Pathways does valuations for 2 to 4 practices per week in all specialty areas. If you want to increase the value of your practice, I would advise you to develop a business plan that shows future growth (for example, by signing new managed care contracts) and minimizes the past (especially if the trend of your revenues has been stable or declining until recently).

To close on a positive note: After reading this report, I hope you'll agree with me that the future is not only full of challenge for physicians, but is loaded with opportunity as well. Remember the NEW factors that positively affect your practice: improved procedures made possible through technology, an aging population that requires more care, and the increasing belief among both government and employers that health care and health care coverage is an inalienable right.

Instead of seeing more and more patients for fewer dollars, managed care can bring increased revenues for those doctors who are flexible and aggressive enough to accept the challenge of delivering greater value to their patients, by providing more service and satisfaction for the money.

A useful analogy is the automobile. We all have nostalgia for the cars we drove in our youth. But in truth the automobile is a much better machine today than it ever was in the past: more fuel-efficient, safer, and a far better value for what it delivers. Patients, employers and government are demanding similar increases in the quality and efficiency of medical care. Physicians can and will prosper by meeting these challenges with energy and creativity.

\*Mr. Eberhard has over 25 years experience in management and consulting in healthcare. Most recently, as president and founder of Medical Pathways, he has been instrumental in a number of transactions which have helped physicians make their practices more efficient, increase the number of patients, and in many cases improve the value of the practice for a merger or acquisition partner.

Prior to founding Medical Pathways in 1988, Mr. Eberhard held positions as a senior executive with a national non-profit hospital group and a leading tertiary care center (in Southern California) with responsibility for physician ventures and business development. He holds no fewer than three Master's Degrees (including an MBA from UCLA), and is a graduate of the University of San Francisco.